

Low Carbon Fuel Standard, Cap and Trade, and Public Benefits Revenues

State Regulations and Council Policies

This attachment provides an overview of the State regulations and Council policies applicable to the revenues received as a result of:

- The State-mandated participation of the City's gas and electric utilities in the Western Climate Initiative Cap and Trade Program (Gas and Electric Cap and Trade revenues)
- The City's electric utility's participation in the State's Low Carbon Fuel Standard program for the electricity it serves to electric vehicles (LCFS revenues)
- The revenues the State mandates the City's electric utility collect for public purpose programs and the gas utility's public purpose program requirements (Gas and Electric Public Benefits)

Electric Cap and Trade

Regulatory requirements: 17 Code of California Regulations (CCR) 95892

- Revenue must be used "for the primary benefit of retail electricity ratepayers of each electrical distribution utility, consistent with the goals of AB 32, and may not be used for the benefit of entities or persons other than such ratepayers." (17 CCR sec. 95892(d)(3)).
- Revenues subject to any limitations imposed by the governing body of the utility, as well as those listed below.
- Revenue must be used for:
 - Renewable energy (including with energy storage), as described in 95892(d)(3)(A);
 - Energy efficiency or other projects that reduce energy demand
 - Fuel switching, including zero emissions vehicles (ZEVs) or ZEV infrastructure, active transportation, or public transportation
 - Other greenhouse gas (GHG) emissions activities for which the electrical distribution utility can demonstrate GHG emission reductions, including but not limited to sulfur hexafluoride (SF6) reduction, wildfire risk reduction, or forest carbon sequestration
 - Non-volumetric return to ratepayers (e.g. a climate credit)
 - Administrative overhead and educational programs of the above uses

Council policy: Resolution 10077¹, approved October 3, 2022

The Council resolution, originally approved in 2012 and amended in 2022, permits:

- Purchases of renewable energy
- Investment in energy efficiency
- Fuel switching from other fuels to electricity
- Investment in other carbon reduction activities
- Rebates to electric ratepayers

¹ Resolution 10077, October 3, 2022, *Resolution of the Council of the City of Palo Alto Amending the City's Policy on the Use of Freely Allocated Allowance Under the State's Cap-and-Trade Program and Authorizing the City Manager to use \$1.25 million from the Gas Utility Cap and Trade Reserve for the Advanced Heat Pump Water Heater program*, <https://portal.laserfiche.com/Portal/DocView.aspx?id=38224&repo=r-704298fc>

All uses of these funds will be reviewed for compliance with applicable State law before implementing new programs.

Examples of permissible uses of Electric Cap and Trade Funds:

Use category	Examples
Renewable energy	<ul style="list-style-type: none"> • Buying energy via power purchase agreement (PPA) from utility-scale renewable generators outside Palo Alto • Prepayments of PPAs to reduce overall costs • Buying local renewable energy (e.g. via Palo Alto CLEAN) from solar installations or solar + battery microgrids • Incentives / rebates for local renewable energy (e.g. solar rebates), including local solar + battery microgrids
Energy efficiency	<ul style="list-style-type: none"> • Rebates or programs to install efficient equipment in buildings, including “Efficiency as a Service” programs
Fuel switching	<ul style="list-style-type: none"> • Rebates or programs to replace gas equipment in buildings with electric equipment, • Zero emissions vehicle rebates and charging/fueling infrastructure
Other carbon reduction	<ul style="list-style-type: none"> • Replacing SF6 in utility equipment (e.g. transformers) • Active transportation (e.g. walking, biking, e-bikes, e-scooters) • Public transit
Rebates	<ul style="list-style-type: none"> • Climate Credit to some or all customers in Palo Alto

History of Council policy adoption and revenue allocation

- December 10, 2012: Council adopts Resolution 9307² on use of Cap and Trade revenue for the Electric Utility. Authority to designate use of revenue was delegated to the City Manager, except for customer rebates, which were required to be approved by Council. In the discussion staff recommended that the revenues be used to fund renewable energy and energy efficiency programs already planned by the utility.
- FY 2012 – FY 2020: 100% of funds were used for renewable energy and energy efficiency.
- August 4, 2020: Council approved use of some Cap and Trade revenue for local decarbonization.³ Revenue was to be transferred to a Cap and Trade reserve until designated for use under the Council-adopted policy.
- October 3, 2022: Council adopts Resolution 10077 updating the use of Cap and Trade revenue policy for the Electric Utility to explicitly include fuel switching from other fuels to electricity.

² Resolution 9307, December 10, 2012, *Resolution of the Council of the City of Palo Alto Adopting the Cap-and-Trade Revenue Utilization Policy for the Use of Revenues From the Sale of Allocated Allowances in California's Greenhouse Gas Cap-and-Trade Auctions*, <https://portal.laserfiche.com/Portal/DocView.aspx?id=9550&repo=r-704298fc>

³ Staff Report 11556, August 24, 2020: <https://www.cityofpaloalto.org/civicax/filebank/blobdload.aspx?BlobID=78046>

Gas Cap and Trade

Regulatory requirements: 17 CCR 95893

- Revenue must be used “for the primary benefit of retail gas ratepayers of each electrical distribution utility, consistent with the goals of AB 32, and may not be used for the benefit of entities or persons other than such ratepayers.” (17 CCR sec. 95893(d)(3))
- Revenues subject to any limitations imposed by the governing body of the utility, as well as those listed below.
- Revenue must be used for:
 - Energy efficiency and other projects that reduce energy demand
 - Other GHG emissions activities, for which the natural gas supplier can demonstrate GHG emission reductions, including but not limited to reductions in emissions of uncombusted natural gas not required by mandates
 - Non-volumetric return to ratepayers (e.g. a climate credit)
 - Administrative overhead and educational programs for the above uses

Council policy: Resolution 10077⁴, approved October 3, 2022

The Council resolution, originally approved in 2015 and amended in 2022, permits:

- Investment in energy efficiency
- Purchases of cost effective renewable biogas
- Fuel switching from natural gas to electricity that reduces greenhouse gas emissions
- Investment in other carbon reduction activities including system maintenance or replacement to reduce fugitive gas emissions;
- Non-volumetric rebates to electric ratepayers

It expresses a preference for the use of revenues for GHG-reducing activities. All uses of these funds will be reviewed for compliance with applicable State law before implementing new programs.

Examples of permissible uses of Gas Cap and Trade Funds:

Use category	Examples
Energy efficiency	<ul style="list-style-type: none"> • Rebates or programs to install efficient equipment in buildings, including “Efficiency as a Service” programs
Purchases of cost-effective biogas	<ul style="list-style-type: none"> • Purchases of cost-effective biogas for the gas portfolio
Fuel switching	<ul style="list-style-type: none"> • Rebates or programs to replace gas equipment in buildings with electric equipment,
Other carbon reduction	<ul style="list-style-type: none"> • Leak detection and repair more frequent than mandated
Rebates	<ul style="list-style-type: none"> • Climate Credit to some or all customers in Palo Alto

History of Council policy adoption and revenue allocation

⁴ Resolution 10077, October 3, 2022, *Resolution of the Council of the City of Palo Alto Amending the City’s Policy on the Use of Freely Allocated Allowance Under the State’s Cap-and-Trade Program and Authorizing the City Manager to use \$1.25 million from the Gas Utility Cap and Trade Reserve for the Advanced Heat Pump Water Heater program*, <https://portal.laserfiche.com/Portal/DocView.aspx?id=38224&repo=r-704298fc>

- January 26, 2015: Council adopts Resolution 9487⁵ on the use of Gas Cap and Trade revenue. The policy expresses a preference for the use of revenues for GHG-reducing activities.
- October 3, 2022: Council adopts Resolution 10077 updating the use of Cap and Trade revenue policy for the Gas Utility to explicitly include fuel switching from other fuels to electricity. At that time Council also allocated \$1.25 million for the Advanced Heat Pump Water Heater Pilot Program.
- April 15, 2024: Council allocated an additional \$846K to the Advanced Heat Pump Water Heater Pilot Program

Low Carbon Fuel Standard

Regulatory requirements: 17 CCR 95483(c), 95491(d)(3)(A) California Air Resources Board (CARB) Guidance Document 20-03

- 25% of credit revenue must be contributed to the statewide Clean Fuel Reward program
- 50% of remaining credit revenue must be used for low-income individuals
- The remaining credit revenue must be used to benefit current or future EV drivers
- CARB strongly encourages revenue collected from a specific sector (e.g. residential) to be used for projects serving that sector

Council policy: Resolution 9871, December 2, 2019⁶

The Council resolution, originally approved in 2016 and amended in 2019, permits the following for the use of funds from the sale of LCFS credits obtained due to serving electricity to EVs:

- EV charger infrastructure focused on multi-family, including utility connection fees
- EV rebates, including e-bikes and e-scooters
- Rate incentives to lower the cost of EV charging or encourage off-peak charging
- EV demand response
- Education and outreach

All uses of these funds will be reviewed for compliance with applicable State law before implementing new programs.

⁵ Resolution 9487, January 26, 2015, *Resolution of the Council of the City of Palo Alto Amending the Cap-and-Trade Revenue Utilization Policy to Cover the Use of Freely Allocated Allowances for the Gas and Electric Utilities*, <https://portal.laserfiche.com/Portal/DocView.aspx?id=10165&repo=r-704298fc>

⁶ Resolution 9871, December 2, 2019, *Resolution Amending Utility Rate Schedule E-15 (Electric Service Connection Charges), and Approving Updates to the City's Program for use of Revenues from the Sale of Low Carbon Fuel Standard Credits*, <https://portal.laserfiche.com/Portal/DocView.aspx?id=18339&repo=r-704298fc>

Examples of permissible uses of LCFS Funds from serving electricity to EVs:

Use category	Examples
Low-income projects and programs	<ul style="list-style-type: none"> • EV charging infrastructure • EV rebates • Public transit and active transportation (bikes, walking) • E-mobility (e.g. e-bikes, e-scooters, EV sharing and rideshare) • Bill credits to reduce the cost of EV charging
Use for the benefit of current and future EV owners	<ul style="list-style-type: none"> • EV charging infrastructure • EV rebates • Bill credits to reduce the cost of EV charging

The policy also includes provisions related to the LCFS credits received for serving compressed natural gas (CNG), which must be used to promote CNG vehicle adoption, including:

- Capital and maintenance costs of the City's CNG station
- Activity to dispense carbon neutral CNG (e.g. offsets or renewable natural gas)
- Reducing the CNG retail charge rate

History of Council policy adoption and revenue allocation

- October 24, 2016: Council adopts a policy on the use of Low Carbon Fuel Standard revenue.⁷ It included an initial spending plan and gave the City Manager authority to make changes.
- December 2, 2019: Council approves Resolution 9871 updating the policy to include rebates for connection fees (e.g. the cost of transformer upgrades)

Electric Public Benefits*Regulatory requirements: State Public Utilities Code Section 385 (AB 1890, 1996)*

- Publicly owned utilities must impose a surcharge on all electricity sales to fund:
 - (1) Cost-effective demand-side management services to promote energy-efficiency and energy conservation
 - (2) New investment in renewable energy resources and technologies consistent with existing statutes and regulations which promote those resources and technologies.
 - (3) Research, development and demonstration programs for the public interest to advance science or technology which is not adequately provided by competitive and regulated markets.
 - (4) Services provided for low-income electricity customers, including but not limited to, targeted energy efficiency service and rate discounts.

Council policy: FY 1998 Rate Setting Process, spring 1997 and FY 1999 Budget, spring 1998

⁷ Staff Report ID#7301, October 24, 2016:

<https://portal.laserfiche.com/Portal/DocView.aspx?id=51391&repo=r-704298fc&>

On May 5, 1997 Council approved modifications to the electric utility rates to separate them into distribution, supply, and public benefits charges, as mandated by law, and as described in City Manager's Report (CMR) 219:97⁸. The public benefits charge was only 1.6% of revenues when it took effect July 1, 1997, below the 2.85% of revenues mandated by law, but in its motion to approve the FY 1999 Budget on June 22, 1998 the Council approved a UAC and Finance Committee recommendation to increase Public Benefits spending to 2.85% as described in CMR 237:98⁹. A Public Benefits Reserve was also created to hold any unspent funds from the Public Benefits charge.

Council has approved plans for spending of electric public benefits funds in various forms since then. The most current approved plan for electric public benefit spending was adopted May 3, 2021, setting 10-year electric energy efficiency goals.¹⁰

Examples of permissible uses:

Use category	Examples
Cost-effective energy efficiency and conservation	<ul style="list-style-type: none"> • Rebates or programs to install efficient equipment in buildings, including "Efficiency as a Service" programs • Rebates or programs to replace gas equipment in buildings with electric. • E-bikes or e-scooters as transportation energy efficiency
Renewable energy	<ul style="list-style-type: none"> • Buying energy via power purchase agreement (PPA) from utility-scale renewable generators outside Palo Alto • Prepayments of PPAs to reduce overall costs • Buying local renewable energy (e.g. via Palo Alto CLEAN) from solar installations or solar + battery microgrids • Incentives / rebates for local renewable energy (e.g. solar rebates), including local solar + battery microgrids
Research and development	<ul style="list-style-type: none"> • Building envelope improvements to reduce heat loss
Low-income services	<ul style="list-style-type: none"> • Utilities Residential Energy Assistance Program, which does direct installation of efficiency measures in homes • Rate or bill discounts for low-income customers • Low-income building or vehicle electrification programs (including EV charging) that reduce bills for income-qualified customers compared to use of gas or gasoline

Gas Public Benefits

Regulatory requirements: State Public Utilities Code Section 890 (AB 1002, 2000)

- A surcharge must be imposed on all methane gas consumed in California to fund:
 - low-income rate assistance programs,
 - low-income energy efficiency programs,

⁸ City Manager's Report 219:97, Finance Committee, May 5, 1997, *Proposed Electric Fund Rate Increase, Establishment of Unbundled Rates and New Commercial Rate Options, and Calaveras Reserve Proposal*, <https://portal.laserfiche.com/Portal/DocView.aspx?id=60628&repo=r-704298fc>

⁹ City Manager's Report 237:98, May 19, 1998, *Proposed Electric Public Benefits Programs for Fiscal Year 1998-1999*, <https://portal.laserfiche.com/Portal/DocView.aspx?id=60632&repo=r-704298fc>

¹⁰ Staff Report ID#12068, May 3, 2021: <https://www.cityofpaloalto.org/files/assets/public/v/1/agendas-minutes-reports/reports/city-manager-reports-cmr/yr-archive/2021/id-12068.pdf>

- cost-effective energy efficiency and conservation activities, and
- public interest research and development not adequately provided by the competitive and regulated markets.
- Municipalities that offer home weatherization services, low-income customer rate assistance or programs similar to those set forth above are not required to collect the surcharge.

Council policy: FY 1997 Budget, June 24, 1996

In its motion to approve the FY 1997 Budget on June 24, 1996 the Council approved a UAC and Finance Committee recommendation to approve a new Demand Side Management (DSM) policy as described in City Manager's Report (CMR) 209:96. CMR:209:96¹¹ recommended a "policy for allocation of (between .75% and 1.25% of revenues) to the environmentally friendly and DSM programs, with proposed program details to be provided to the UAC for review and comment."

Council has approved plans for spending of gas public benefits in various forms since then. The most current approved plan for gas public benefit spending was adopted April 3, 2017, setting 10 year gas efficiency goals.¹²

Examples of permissible uses:

Use category	Examples
Low-income rate assistance programs	<ul style="list-style-type: none"> • Utilities Rate Assistance Program
Low-income energy efficiency programs	<ul style="list-style-type: none"> • Utilities Residential Energy Assistance Program, which does direct installation of efficiency measures in homes
Cost-effective energy efficiency and conservation	<ul style="list-style-type: none"> • Building envelope improvements to reduce heat loss
Research and Development	<ul style="list-style-type: none"> • Building electrification resulting in reduced gas utility costs (e.g. block electrification to prevent gas main replacement)

¹¹ City Manager's Report 209:96, City Council, April 18, 1996, *Budget Issue: New Demand Side Management Program*, <https://portal.laserfiche.com/Portal/DocView.aspx?id=60592&repo=r-704298fc>

¹² Staff Report ID#7862, April 3, 2017: https://www.cityofpaloalto.org/files/assets/public/v/1/agendas-minutes-reports/reports/city-manager-reports-cmrs/year-archive/2017/final-staff-report-id-7862_update-of-ten-year-gas-efficiency-goals.pdf